STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 2001-410

September 5, 2001

BANGOR HYDRO-ELECTRIC COMPANY
Request for Approval of Alternative Rate Plan

ORDER REJECTING STANDARD OFFER PROPOSAL

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. SUMMARY

In this Order, we reject Bangor Hydro-Electric Company's (BHE) proposal to provide standard offer service as part of its Alternative Rate Plan (ARP). We direct BHE to file an ARP proposal consistent with our order in Docket No. 2000-663 and that does not contain an energy supply component.

II. PROCEDURAL HISTORY

In our order approving the proposed merger between BHE and Emera, Inc. (Emera), BHE was directed to file an Alternative Rate Plan (ARP) proposal within two months of the closing of the merger with Emera or by June 30, 2001, whichever was earlier. *Bangor Hydro-Electric Company; Maine Electric Power Company, Inc.; Chester SVC Partnership; and Emera, Inc., Request for Approval of Reorganization (Joint Petition),* Docket No. 2000-663, Order Rejecting Revised Stipulation and Approving Stipulation (Jan. 5, 2001). On June 15, 2001, BHE filed a letter with the Commission stating that it intended to file a comprehensive 4-year ARP covering both distribution service and standard offer service. BHE also requested that it be given an extension until July 31, 2001 to file its proposal to allow the Company sufficient time to develop a 4-year plan for standard offer service. In its letter, BHE also indicated that given the volatility in the power supply market, "the specific ARP pricing BHE plans to offer will likely only be available for a limited time" and therefore the Commission should act promptly on the Company's proposal.

A Notice of Proceeding granting BHE's request for extension and providing interested persons with an opportunity to intervene was issued on June 21, 2001. The Office of Public Advocate (OPA), the Industrial Energy Consumers Group (IECG), International Paper (IP), Georgia Pacific Corporation (GP), Independent Energy Producers of Maine (IEPM) and Competitive Energy Services (CES) filed petitions to intervene. Those petitions were granted in a Procedural Order dated July 18, 2001.

In light of the Company's statements concerning the need for quick action on the power supply component of its proposal and given the significant legal and policy issues raised by the Company's proposal, the Examiner established an expedited schedule which called on the parties to brief the legal and policy issues raised by the Company's proposal to be the standard offer provider in its service territory for the next four years as part of its ARP.[1] The OPA, IEPM, IECG and CES filed briefs in opposition to the Company's proposal. The Company filed a brief responding to the Intervenors' arguments on July 31, 2001 and on August 7, 2001 the OPA and the IECG filed reply briefs.

III. BACKGROUND

On March 1, 2000, pursuant to the provisions of the Electric Industry Restructuring Act, 35-A M.R.S.A. § 3201, generation service was deregulated and Maine consumers were given the right to purchase generation service directly from competitive electricity providers. The Restructuring Act also requires, however, that standard offer service be available to all consumers through March 1, 2005.[2] The Commission promulgated Chapter 301 of its rules to establish the terms of standard offer service as well as the bid process to be utilized to select standard offer service providers for each transmission and distribution utility's service territory.

In the Fall of 1999, pursuant to the provisions of Chapter 301, the Commission solicited bids to provide service to BHE's three classes of standard offer customers. In an Order dated October 25, 1999, the Commission rejected all the bids received for BHE service territory and solicited a second round of proposals. By Order dated December 3, 1999, the Commission again rejected all bids for providing standard offer service to the BHE service territory. As a consequence of the bid rejection, we directed BHE, pursuant to Chapter 301, Section 8(B), to provide standard offer service to all customer classes using power procured from the wholesale market for the period of March 1, 2000 through February 28, 2001.

On October 2, 2000, the Commission issued a Request for Bids (RFB) to provide standard offer service to customers in BHE's service territory for the period beginning March 1, 2001. On December 22, 2000, the Commission found that bids received in response to the RFB were inadequate due to current price spikes in the New England wholesale electricity market and concluded that it would not be in the public interest to accept any of the bids. *Maine Public Utilities Commission, Standard Offer Bidding Process,* Docket No. 2000-808, Order Terminating Bid Process and Adopting Alternative Selection Processes (Dec. 22, 2000). The Commission also directed BHE to explore wholesale power supply options in order to provide standard offer service.

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[1] As part of the expedited schedule, Intervernor's initial briefs were filed prior to the filing of the Company "All-In ARP" proposal and were based on the Company's written and oral summaries of its "All-In ARP" proposal.

[2] Standard offer service means electric generation service provided to any electricity consumer who does not obtain electric generation service from a competitive electricity provider or who has terminated service from a competitive electricity provider. MPUC Rules, ch. 301, section 1(A)(6).

BHE ultimately entered into several supply arrangements of differing time periods, which we found to be prudent. We designated BHE as the standard offer provider for all classes for the 12-month period beginning March 1, 2001. We specifically noted at that time, however, that although BHE had entered into supply contracts beyond March 1, 2002, we made no decision on whether BHE would provide standard offer service after that date.[3] *Maine Public Utilities Commission, Standard Offer Bidding Process,* Docket No. 2000-808, Order Directing Bangor Hydro-Electric Company to Contract for Wholesale Power Supply and Establishing Standard Offer Prices (Part II)(Mar. 7, 2001).

In light of a decline in the forward price for electricity, the Commission recently directed Staff to issue requests for standard offer proposals for BHE's residential and small non-residential class. The Commission did not take a similar action for the medium and large classes because it concluded that given current market conditions, competitive providers should be able to offer attractive prices relative to current standard offer rates, and it did not want to inhibit progress towards customers leaving the standard offer for the competitive market.[4] *Public Utilities Commission, Standard Offer Bidding Procedure,* Docket No. 2001-399, Order Regarding Standard Offer Bid Process (July 18, 2001).

IV. POSITIONS OF THE PARTIES

A. Description of the BHE Proposal

On July 31, 2001, BHE filed its "All-In ARP" proposal. The "All-In ARP" is made of three distinct but related components: the "D-ARP" covering the distribution component of service; the "SC-ARP" governing stranded costs; and a "Standard Offer ARP." According to the Company, these three component pieces are inter-related and inseparable. The Company's "All-In ARP" would run from March 1, 2002 through February 28, 2006.

Under the Company's "Standard Offer ARP," BHE would be appointed as the standard offer provider for BHE's small and medium customer classes for the 4-year "All-In ARP" period. The Company would not, however, provide standard offer service to the large customer class. The Company stated that as part of its "All-In ARP" proposal it was willing to provide service at 5.5 cents per kWh subject to revision at the time a detailed term sheet was executed with its "preferred supplier."

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[3]For the period beginning March 1, 2001, prices were established for BHE's residential/small non-residential customer class at $0.073/kWh and for the BHE medium non-residential customer class for summer at $0.08498/kWh and non-summer at $0.06889/kWh.

[4]With the greater load migration concerns for the medium and large classes, it is also less clear that it would be that advantageous to solicit bids for those classes so far in advance of the March 1, 2002 start date.

BHE indicated that it intended to meet its standard offer obligation through a combination of new power supply contracts and existing QF and standard offer supply contracts and diesel generation. Under the Company's proposal, it would bear the risk of any profit or loss on standard offer service and would have the right to reduce standard offer prices for any customer or rate class during the term of the ARP.

B. Intervenors' Arguments[5]

The Intervenors argue that while 35-A M.R.S.A. § 3212 allows the Commission to designate BHE as a default service provider, default service by a T&D utility under section 3212 is a last resort and that before the utility can be designated as the default service provider, the Commission must go through the standard offer bid process and determine that no bids are acceptable. The Commission's December, 2000 bid process for standard offer service in March, 2001 does not provide a sufficient basis for awarding default service for the next four years.

The Intervenors also argue that since the "All-In ARP" plan provides that BHE would retain certain existing rights to generation service and would obtain additional load to meet its standard offer obligations, the plan would violate the provisions of 35-A M.R.S.A. § 3204(5) which prohibit a utility from owning, having a financial interest in, or otherwise controlling generation or generation-related assets.

The Intervenors further assert that the BHE ARP proposal would violate the provisions of 35-A M.R.S.A. § 3205(2) which prohibit a T&D utility from selling energy and capacity at retail. In addition, the Intervenors argue that the BHE proposal would allow BHE to circumvent § 3205(2)(B), which limits the sales of a T&D utility's affiliate to 33% of the total kWh in the T&D's service territory and to no more than 20% of the standard offer load. Allowing BHE to bear the financial risk/reward of the standard offer service, according to the Intervenors, is not a trivial matter and would greatly affect BHE's behavior towards other competitive suppliers.

Finally, the IECG argues that BHE's proposal to provide standard offer to its small and medium classes but not to its large customer class is discriminatory and would thus violate § 702 of Title 35-A.

C. BHE's Response

The Company counters that under its "All-In ARP" proposal it is merely proposing to continue in its current role as the provider of default standard offer service. BHE argues that, if the Intervenors are correct in their arguments, then BHE must

[5]As noted previously, Intervenor briefs were filed by the OPA, the IECG, the IEPM and CES. All Intervenors opposed BHE's proposal and most of the Intervenors presented similar arguments. For purposes of this summary, the Intervenors' arguments are presented on a consolidated basis.

already be violating the Restructuring Act. The Company notes that the Commission has already gone out to bid twice for standard offer service in BHE's territory. On each occasion the process has failed to yield an acceptable standard offer bid.

The Company acknowledges that whether these past failures provide an adequate basis to designate BHE as the standard offer service provider for the next four years under its "All-In ARP" now appears to be moot since the Commission has recently issued a new bid for standard offer service. The Company goes on to state that the Commission now will be able to judge for itself whether any alternatives to BHE's proposal are acceptable. If the Commission once again finds that none of the bids is acceptable, the Commission will have an adequate basis to accept the Company's proposal for continuing as a standard offer provider.

The Company counters the arguments that retention of the QF output to meet its standard offer obligation would violate § 3204 by noting that § 3204(4) specifically excepts from the sale requirements capacity and energy that is necessary to perform its duties as a transmission and distribution utility in an efficient manner; since providing standard offer service is part of a T&D service and since retention of the capacity and energy would allow it to perform this duty more efficiently, retention of this capacity is proper.

Finally, BHE argues that its proposal to provide standard offer service to the small and medium classes but not to the large customer class is not discriminatory since § 3212(5) allows standard offer service to be provided on different terms to different classes. Even if it could be construed as discriminatory, the discrimination is justified by the lack of attention given to small customers by competitive providers when compared to the attention given large customers.

V. DECISION

The standard offer bid process in BHE's service territory has thus far been less than an overwhelming success. We appreciate BHE's efforts to create an attractive alternative, but for the reasons set forth below, we reject BHE's standard offer ARP proposal.

The Legislature has clearly committed the State to open the Maine retail generation market to the forces of competition. 35-A M.R.S.A. § 3201 *et. seq.* As part of the restructuring process and to ensure a level competitive playing field, the Legislature restricted the role that T&D utilities could play in the generation sector. First, investor-owned utilities were required, with certain limited exceptions, to divest all their generation assets and all their generation-related business activities by March 1, 2000. As of that date, T&D utilities were prohibited from owning or having a financial interest in, or otherwise controlling, generation-related assets. Second, investor-owned utilities were prohibited from selling energy and capacity to any retail consumer of electricity. 35-A M.R.S.A. §§ 3205 and 3206. While an affiliated competitive provider of a T&D utility could sell to retail consumers, very strict codes of conduct governing the relationship between the T&D utility and the affiliated competitive electricity provider were established and the amount of load that the affiliated competitive provider of a large T&D could serve within the T&D utilities' service territory was limited.

We agree that the Restructuring Act does not totally prohibit a utility from participating in the standard offer bid process. The circumstances under which a T&D utility can participate, however, are quite specific and limited. Specifically, the Restructuring Act provides that:

> Notwithstanding any other provision of this Title, the commission may, in the event that the commission receives no bids to provide standard offer service in a transmission and distribution utility's territory or the commission determines that the bids it receives are inadequate or unacceptable, require the transmission and distribution utility to arrange and to provide for default service.

35-A M.R.S.A. § 3212.

We do not view the distinction made by the Legislature between "standard offer service" and "default service" as accidental or immaterial. To award default service to the utility, the Commission must first conduct a bid process and either not receive any bids or not receive any acceptable bids. It was on this basis that we designated BHE as the default service provider both in 2000 and 2001.

Our decisions in Docket Nos. 99-111 and 2000-808, which rejected the standard offer bids we received in response to our bid process and designated BHE as the default service provider, should not be construed as a determination that the competitive market model established by the Legislature is unworkable. In fact, in our order rejecting standard offer bids last December, we noted that our process for March 1, 2001 standard offer bids appeared to be poorly timed because it coincided with extraordinary high natural gas prices and an adverse decision by the FERC concerning ICAP deficiency charges. We concluded (correctly, as it happened) that it was likely that this price spike was transient and that wholesale prices would moderate in the future. *Maine Public Utilities Commission, Standard Offer Bidding Process,* Docket No. 2000-808, Order Terminating Bid Process and Adopting Alternative Selection Processes at 3 (Dec. 22, 2000).

In our order in Docket No. 2001-399 issued on July 18, 2001, we noted that conditions in the wholesale market had in fact improved since December, 2000, and consistent with the requirements of 35-A M.R.S.A. § 3212, we initiated a bid process for the provision of standard offer service for the period beginning March 1, 2002 for BHE's residential and small non-residential class. *Public Utilities Commission, Standard Offer Bidding Process,* Docket No. 2001-399, Order Regarding Standard Offer Bid Process at 4 (July 18, 2001). Pursuant to the provisions of this Order and to the provisions of Chapter 301 of the Commission's Rule, the Commission issued a Request for

Proposals to Provide Standard Offer Service to Electric Customers in Bangor Hydro-Electric Company's Service Area (RFP) on July 19, 2001.

The Commission has received bids from interested competitive service providers in response to our RFP. At this point, it would be premature to judge whether these bids will produce standard offer service prices which we find acceptable.[6] After we have gone through the bid process, it is possible that we may determine that the bids are not acceptable and that BHE should continue to be required to provide default standard offer service. Such a conclusion, however, cannot be made at this time. Therefore, the legal premise which would allow BHE to provide default standard offer service has not been satisfied. We thus conclude that BHE's proposal that it be appointed as the standard offer provider for the next four years as part of its "All-In ARP" should be rejected. BHE should file an ARP proposal without a power supply component on a schedule as determined by the Examiner.

In rejecting BHE's proposal at this time, we do not address the issue of whether it would ever be lawful to include a profit incentive mechanism as part of a requirement that the T&D utility provide default standard offer service. Should we require BHE to provide default service in the future, however, we note in advance the strong reservations we would have in allowing a T&D to profit from the provision of default standard offer service given the Legislature's commitment to an open competitive market, the specific statutory restrictions imposed by the Legislature on a T&D company's role in the competitive generation market, and the possible chilling effect that allowing the incumbent T&D utility to provide generation service on a profit basis could have on the market. In addition, given the need for very quick Commission action on power supply/standard offer issues necessitated by volatility in the wholesale supply market and what we see as both complex and unrelated issues inherent in a T&D ARP plan, any future proposal concerning the provision of standard offer service by BHE should be made in the context of the standard offer process and not in this ARP case.

Accordingly, it is

O R D E R E D

1. That Bangor Hydro-Electric Company's proposal of July 31, 2001 to provide standard offer service as part of the Company "All-In ARP" is rejected; and

2. That BHE shall file an ARP proposal consistent with our Order in Docket No. 2000-663 without an energy supply component by a date to be established by the Examiner in this matter.

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[6] A standard offer bid may also contain conditions that render it unacceptable for reasons other than price.

Dated at Augusta, Maine, this 5th day of September, 2001.

BY ORDER OF THE COMMISSION

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Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR: Welch
Nugent
Diamond

THIS DOCUMENT HAS BEEN DESIGNATED FOR PUBLICATION

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.

2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Appellate Procedure.

3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

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